

1991

# Insurance Coverage for Patent Infringement

Thomas J. Stueber

Follow this and additional works at: <http://open.mitchellhamline.edu/wmlr>

## Recommended Citation

Stueber, Thomas J. (1991) "Insurance Coverage for Patent Infringement," *William Mitchell Law Review*: Vol. 17: Iss. 4, Article 3.  
Available at: <http://open.mitchellhamline.edu/wmlr/vol17/iss4/3>

This Article is brought to you for free and open access by the Law Reviews and Journals at Mitchell Hamline Open Access. It has been accepted for inclusion in William Mitchell Law Review by an authorized administrator of Mitchell Hamline Open Access. For more information, please contact [sean.felhofer@mitchellhamline.edu](mailto:sean.felhofer@mitchellhamline.edu).

© Mitchell Hamline School of Law

## INSURANCE COVERAGE FOR PATENT INFRINGEMENT

THOMAS J. STUEBER†

INTRODUCTION .....	1055
I. BACKGROUND .....	1056
A. Patent Infringement .....	1057
1. How a Patent is Infringed .....	1057
2. Who May Be Liable for Patent Infringement ....	1059
a. Direct Infringement .....	1059
b. Contributory Infringement .....	1059
c. Active Inducement of Infringement .....	1060
B. The Commercial General Liability Policy .....	1061
1. Definition of Advertising Injury and Liability ....	1061
2. Exclusions .....	1062
C. Interpreting an Insurance Policy .....	1063
1. Interpreting the Coverage Provided by the Policy ..	1063
2. Interpreting the Duty to Defend .....	1065
3. The Duty to Provide Independent Counsel .....	1068
II. ANALYSIS .....	1069
A. Early Attempts to Obtain Coverage .....	1069
B. The Intex Case .....	1073
C. Applying Intex .....	1074
1. Does Patent Infringement "Arise" from Advertising Activity? .....	1074
2. Is Patent Infringement "Unfair Competition"? ...	1079
CONCLUSION .....	1082

### INTRODUCTION

A recent California case may dramatically affect patent litigation throughout the country. In *Intex Plastics Sales Co. v. United*

---

† Thomas J. Stueber is an attorney at Kinney & Lange, P.A., where he practices in the areas of patent, trademark and copyright litigation. This article reflects only the present opinions and interpretations of the author, which should not be attributed to Kinney & Lange, nor to any of its present or former clients. Mr. Stueber received his A.B. in History from Washington University in St. Louis in 1984 and his J.D. from Hamline University School of Law in 1988.

*National Insurance Co.*,<sup>1</sup> a United States district court decided that an accused patent infringer may look to its Commercial General Liability (CGL) insurance policy for both indemnity and attorneys' fees.<sup>2</sup>

The court found coverage for patent infringement under the CGL policy's coverage for "Advertising Injury." It interpreted the terms "piracy" and "unfair competition," which were included in the definition of "Advertising Injury," to cover patent infringement. Consequently, the insurer was obligated not only to indemnify the accused infringer for any damages it may be obligated to pay, but also to pay the insured's legal expenses in defending the patent infringement suit.

The decision in *Intex* has important ramifications for emerging companies. Many small companies simply cannot afford the cost of defending a patent infringement suit, and they are forced either to settle the case on unfair terms or to go out of business. The result is a stifling of fair competition, a decrease in innovation, and a general weakening of the patent system. Providing recourse to an insurance policy will allow small companies to defend patent infringement suits on the merits. For many small companies, the only alternative is to abandon legitimate activities to avoid the expense of litigation. In an area of law known for both its high damage awards and high attorneys' fees, the decision in *Intex* may have significant impact on patent litigation by allowing small companies to vigorously defend patent infringement suits.

## I. BACKGROUND

Before discussing the application of insurance policies to patent infringement, it is essential to understand patent rights and how those rights are infringed. It is also important to understand the basic coverage of the CGL policy and the approach taken by courts in interpreting standardized insurance policies.

---

1. 18 U.S.P.Q.2d (BNA) 1567 (C.D. Cal. Dec. 6, 1990).

2. Specialty insurers offer insurance policies which will reimburse patent owners for the costs of suing an alleged infringer ("Patent Enforcement Litigation Expense Insurance Policies") or policies which will reimburse accused infringers for the cost of defending against a charge of patent infringement ("Patent Infringement Defense Insurance Policies"). The scope of this article is limited to coverage under the CGL policy and does not extend to coverage under these specialized policies.

### A. Patent Infringement<sup>3</sup>

#### 1. How a Patent is Infringed

A patent is a complex legal document which, as required by statute, contains many separate sections. For example, the patent must contain a "specification,"<sup>4</sup> a written description of the invention "in such full, clear, concise, and exact terms as to enable any person skilled in the art to which it pertains . . . to make and use" the invention.<sup>5</sup> Also, the patent usually must contain at least one drawing of the invention.<sup>6</sup> However, for purposes of determining patent infringement, one must look to the patent "claims."

Patent claims are required by 35 U.S.C. § 112 and are "word pictures" which describe exactly what invention the patent covers. The patent claims provide the concise legal definition of the invention. Only the "claims" of a patent are legally enforceable.<sup>7</sup> Infringement can be determined only by evaluating the claims.<sup>8</sup>

The claims "describe and point out the invention by a series of limiting words or phrases" called "limitations."<sup>9</sup> The law is well-settled that, "[t]o establish infringement of a patent, every limitation set forth in a claim must be found in an accused product or process."<sup>10</sup> This concept is sometimes referred to

---

3. In 1982, Congress created the Court of Appeals for the Federal Circuit (CAFC) and granted it exclusive appellate jurisdiction for all patent infringement cases. See 28 U.S.C. § 1295 (1990). The major purpose behind the creation of the CAFC was to alleviate the inconsistencies between the circuits in deciding basic patent issues and to do away with the resulting forum shopping. Prior to the creation of the CAFC, for example, the circuits had different rules on such basic issues as whether patent infringement (and common defenses such as anticipation and obviousness) were questions of law or fact, the burden of proof required for common defenses, and even the order of presentation of evidence. Since there can no longer be conflicts between the circuits in patent cases, the CAFC has effectively become the court of last resort in patent law.

4. 35 U.S.C. § 111(1) (1988).

5. *Id.* § 112.

6. *Id.* §§ 111, 113.

7. "A claim in a patent provides the metes and bounds of the right which the patent confers on the patentee to exclude others from making, using, or selling the protected invention." *Corning Glass Works v. Sumitomo Elec. U.S.A.*, 868 F.2d 1251, 1257 (Fed. Cir. 1989).

8. *Id.* at 1258.

9. *Id.*

10. *Johnston v. IVAC Corp.*, 885 F.2d 1574, 1577-78 (Fed. Cir. 1989); *ZMI Corp. v. Cardiac Resuscitator Corp.*, 844 F.2d 1576, 1578 (Fed. Cir. 1988); *Uniroyal, Inc. v.*

as the "All Elements Rule" or the "All Limitations Rule."<sup>11</sup> The plaintiff bears the burden of proving infringement by a preponderance of the evidence.<sup>12</sup>

Determining patent infringement is a two-step process. The first step is to construe the claims.<sup>13</sup> Construction of the disputed claims may require reference to the specification, the prosecution history,<sup>14</sup> the prior art,<sup>15</sup> and the other claims.<sup>16</sup> Expert testimony, including evidence of how those skilled in the art would interpret the claims, may also be used. Although the ultimate issue of infringement is a question of fact, claim interpretation is a question of law.<sup>17</sup>

The second step "is to decide whether properly interpreted claims encompass the allegedly infringing method."<sup>18</sup> If an accused product does not literally infringe a patent claim, infringement may still be found under a theory known as the "doctrine of equivalents." If a device "performs substantially

Rudkin-Wiley Corp., 837 F.2d 1044, 1054 (Fed. Cir.), *cert. denied*, 488 U.S. 825 (1988).

11. *Johnston*, 885 F.2d at 1577 n.3 (citing 4 D. CHISUM, PATENTS § 18.03[4] (1986)).

12. *Uniroyal*, 837 F.2d at 1054; *Mannesmann Demag Corp. v. Engineered Metal Prods. Co.*, 793 F.2d 1279, 1282 (Fed. Cir. 1986).

13. *See, e.g.*, *Senmed Inc. v. Richard-Allen Medical Indus.*, 888 F.2d 815, 818 (Fed. Cir. 1989); *Corning Glass Works v. Sumitomo Elec. U.S.A.*, 868 F.2d 1251, 1258 (Fed. Cir. 1989); *Grain Processing Corp. v. American Maize-Prods. Co.*, 840 F.2d 902, 908 (Fed. Cir. 1988); *Uniroyal*, 837 F.2d at 1054; *Texas Instruments, Inc. v. United States Int'l Trade Comm'n*, 805 F.2d 1558, 1562 (Fed. Cir. 1986).

14. The "prosecution history," often referred to as the "file wrapper," is the official record of the prosecution of the patent in the United States Patent and Trademark Office. It contains the original patent application and the patent examiner's decision or decisions on the patentability of the invention. If the patent application is rejected (and rejection of a patent application is common), the file wrapper will contain the applicant's response or responses to the examiner, as well as any changes ("amendments") to the claims which are made by the applicant. A review of the file wrapper is essential to determining the scope of the claims of a patent. *See Hughes Aircraft Co. v. United States*, 717 F.2d 1351, 1363 (Fed. Cir. 1983); *Autogiro Co. of Am. v. United States*, 384 F.2d 391, 398 (Cl. Ct. 1967).

15. Generally, prior art consists of patents and printed publications which predate the patent application. To be patentable, an invention must not be disclosed in the prior art, 35 U.S.C. § 102 (1988), or be "obvious . . . to a person having ordinary skill in the art." *Id.* § 103. In patent litigation, it is common for the accused infringer to allege that the patent-in-suit is invalid under either section 102 or section 103.

16. *ZMI Corp. v. Cardiac Resuscitator Corp.*, 844 F.2d 1574, 1580 (Fed. Cir. 1989); *Grain Processing*, 840 F.2d at 908; *Witco Chem. Corp. v. Peachtree Doors, Inc.*, 787 F.2d 1545, 1549 (Fed. Cir.), *cert. dismissed*, 479 U.S. 877 (1986).

17. *Tillotson, Ltd. v. Walbro Corp.*, 831 F.2d 1033, 1037 (Fed. Cir. 1987).

18. *Fonar Corp. v. Johnson & Johnson*, 821 F.2d 627, 631 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1027 (1988).

the same function in substantially the same way to obtain the same result" as the claimed invention, then infringement may be found even if the device does not literally infringe each element of a patent claim.<sup>19</sup> Equivalency is determined in light of the prior art, the patent specification, and the prosecution history.<sup>20</sup>

Each claim of a patent must be considered individually, and not all claims of a patent need to be infringed before the patent is infringed. Infringement of even a single claim requires a finding that the patent is infringed.<sup>21</sup>

## 2. Who May Be Liable for Patent Infringement

In addition to determining *how* a patent is infringed, it is important to consider *who* may infringe a patent. Under 35 U.S.C. § 271, a person may infringe a patent in three ways: by *directly* infringing the patent;<sup>22</sup> by *actively inducing* infringement of the patent;<sup>23</sup> or by *contributorily* infringing the patent.<sup>24</sup>

### a. Direct Infringement

A person directly infringes a patent by *making, using or selling* any patented invention without authority in the United States during the term of the patent.<sup>25</sup>

### b. Contributory Infringement

Contributory infringement is defined in 35 U.S.C. § 271(c):

Whoever sells a component of a patented machine, manufacture, combination or composition, or a material or apparatus for use in practicing a patented process, constituting a material part of the invention, knowing the

19. *Graver Tank & Mfg Co. v. Linde Air Prods. Co.*, 339 U.S. 605, 608 (1950); *see also Wilson Sporting Goods v. David Geoffrey & Assocs.*, 904 F.2d 677, 683 (Fed. Cir.) ("Infringement *may* be found under the doctrine of equivalents if an accused product performs substantially the same overall function or work, in substantially the same way, to obtain substantially the same overall result as the claimed invention." (emphasis by the court)), *cert. denied*, 111 S. Ct. 537 (1990).

20. *Sun Studs, Inc. v. ATA Equip. Leasing, Inc.*, 872 F.2d 978, 986-87 (Fed. Cir. 1989); *Texas Instruments, Inc. v. United States Int'l Trade Comm'n*, 805 F.2d 1558, 1568 (Fed. Cir. 1986).

21. *Intervet Am., Inc. v. Kee-Vet Laboratories, Inc.*, 887 F.2d 1050, 1055 (Fed. Cir. 1989).

22. 35 U.S.C. § 271(a) (1988).

23. *Id.* § 271(b).

24. *Id.* § 271(c).

25. *Id.* § 271(a).

same to be especially made or especially adapted for use in an infringement of such patent, and not a staple article or commodity of commerce suitable for substantial noninfringing use, shall be liable as a contributory infringer.

The United States Supreme Court, in *Aro Mfg. Co. v. Convertible Top Replacement Co.* [hereinafter *Aro II*], defined the "knowing" element of section 271(c) to require a showing "that the alleged contributory infringer knew that the combination for which his component was especially designed was both *patented* and *infringing*."<sup>26</sup> "[T]here can be no contributory infringement without . . . direct infringement."<sup>27</sup>

### c. Active Inducement of Infringement

"Whoever actively induces infringement of a patent shall be liable as an infringer."<sup>28</sup> Section 271(b) of the patent statute "protects against one who aids and abets the direct infringer";<sup>29</sup> its goal is to prevent infringement by imposing liability upon one who intends to infringe by selling a component of a combination patent.<sup>30</sup>

"Establishing an inducement of infringement requires proof of two elements: (1) an act by the defendant knowingly calculated to induce another to infringe, and (2) the actual culmination of the defendant's acts in a direct infringement by another."<sup>31</sup> As previously discussed, the "knowing" element of contributory infringement requires a showing that the defendant knew that the invention was both *patented* and *infringed*.<sup>32</sup> Paragraphs (b) and (c) of section 271 must be read together as allied expressions of the basic underlying concept of contributory infringement. Thus, the "knowing" requirement of section 271(c), as defined in *Aro II*, is at least a threshold requirement under section 271(b).<sup>33</sup>

26. *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 377 U.S. 476, 488 (1964) (emphasis added) [hereinafter *Aro II*], quoted in *Preemption Devices, Inc. v. Minnesota Mining & Mfg. Co.*, 803 F.2d 1170, 1174 (Fed. Cir. 1986).

27. *Deepsouth Packing Co. v. Laitram Corp.*, 406 U.S. 518, 526 (1972).

28. 35 U.S.C. § 271(b) (1988).

29. *Water Technologies Corp. v. Calco Ltd.*, 850 F.2d 660, 668-69 (Fed. Cir.), cert. denied, 488 U.S. 968 (1988).

30. *Jones v. Radio Corp. of Am.*, 131 F. Supp. 82 (S.D.N.Y. 1955).

31. *H.B. Fuller Co. v. National Starch & Chem. Corp.*, 689 F. Supp. 923, 943 (D. Minn. 1988).

32. *Aro II*, 377 U.S. 476, 488 (1964).

33. *Nordberg Mfg. Co. v. Jackson Vibrators, Inc.*, 153 U.S.P.Q. 777, 784 (N.D. Ill. 1967), rev'd on other grounds, 393 F.2d 192 (7th Cir. 1968); see also 4 D. CHISUM,

### B. *The Commercial General Liability Policy*

Interpreting an insurance contract, like any contract, requires analysis of the specific language of the contract. Hence, analysis of "Advertising Injury" under a CGL policy requires reference to the specific language of the policy, and that language varies from policy to policy. However, all of the policies define "advertising injury" in a similar fashion. Nonetheless, reference to the specific policy at issue must be made before determining whether coverage for patent infringement exists under a particular CGL policy.

Insurance policies are complicated documents that attempt to clearly define the scope of protection provided. Generally, a CGL policy contains a "COVERAGE" clause which simply states that "the insurer will pay those sums which the insured becomes legally obligated to pay as damages because of . . . advertising injury."<sup>34</sup> A later section of "DEFINITIONS" defines the term "advertising injury." Finally, a third section of the insurance policy identifies those "EXCLUSIONS" which the insurer explicitly refuses to cover.

#### 1. *Definition of Advertising Injury and Liability*

A typical commercial general liability insurance policy defines "advertising liability" as liability for damages caused by:

- (a) libel, slander or defamation;
- (b) infringement of copyright or of title or of slogan;
- (c) piracy or unfair competition or idea misappropriation under an implied contract; and
- (d) invasion of rights of privacy which occurred during a policy period, and arising out of the named insured's advertising activities.<sup>35</sup>

Some CGL policies define "advertising injury" as "injury arising out of an offense . . . occurring in the course of the named insured's advertising activities, if such injury arises out

---

PATENTS § 17.04[2] (Feb. 1991) ("[T]he *Aro II* requirement that the defendant have some knowledge of the patent as well as the nature of his acts and their consequences would seem to apply equally to Section 271(b) and 271(c).").

34. *Lexington Ins. Co. v. Widger Chem. Corp.*, 805 F.2d 1035 (6th Cir. 1986) (Text in Westlaw), slip op. at 3; *Aetna Casualty & Sur. Co. v. Trans World Assurance Co.*, 745 F. Supp. 1524, 1528 (N.D. Cal. 1990); *National Union Fire Ins. Co. of Pittsburgh, Pa. v. Siliconix Inc.*, 729 F. Supp. 77, 78 (N.D. Cal. 1989).

35. *Aetna Casualty & Sur. Co. v. Centennial Ins. Co.*, 838 F.2d 346, 348 (9th Cir. 1988).



of libel, slander, defamation, violation of right of privacy, piracy, unfair competition, or infringement of copyright, title or slogan.”<sup>36</sup> Similarly, “advertising injury” has been defined as:

- [i]njury arising out of one or more of the following offenses:
  - (a) oral or written publication of material that slanders or libels a person or organization or disparages a person’s or organization’s goods, products or services;
  - (b) oral or written publication of material that violates a person’s right of privacy;
  - (c) misappropriation of advertising ideas or style of doing business; or
  - (d) infringement of copyright, title or slogan.<sup>37</sup>

or:

injury arising out of one or more of the following “offenses” committed in the course of advertising an insured’s goods, products or services:

- (a) oral or written publication of material that slanders or libels a person or organization or disparages a person’s of [sic] organization’s goods, products or services;
- (b) oral or written publication of material that violates a person’s right or [sic] privacy;
- (c) misappropriation of advertising ideas of [sic] style of doing business;
- (d) infringement of copyright, title or slogan; or
- (e) unfair competition.<sup>38</sup>

Similarly, “advertising liability” has been defined as “damages because of libel, slander, defamation, infringement of copyright, title or slogan, piracy, unfair competition, idea misappropriation or invasion of right of privacy arising out of the named insured’s advertising activities.”<sup>39</sup>

## 2. Exclusions

In addition to providing coverage for specific injuries, insurance policies generally exclude liability for injuries arising

36. *John Deere Ins. Co. v. Shamrock Indus., Inc.*, 696 F. Supp. 434, 437 (D. Minn. 1988), *aff’d*, 929 F.2d 413 (8th Cir. 1991).

37. *Id.*; Tobin & Myslis, *The New Commercial General Liability Policy*, INSURANCE LAW 1989 (Minnesota State Bar Association CLE, Sept. 1989).

38. *Shamrock Indus., Inc.*, 696 F. Supp. at 437.

39. *Id.*; see also *Liberty Life Ins. Co. v. Commercial Union Ins. Co.*, 857 F.2d 945, 948-49 (4th Cir. 1988) (defining “advertising activities” as “any advertisement, publicity article, broadcast or telecast and arising out of the Named Insured’s advertising activities”).

from certain acts. The CGL policy is no different. It excludes liability for such things as "infringement of registered trademark, service mark or trade name by use thereof as the registered trademark, service mark or trade name of goods or services sold, offered for sale or advertised, but this shall not relate to titles or slogans."<sup>40</sup>

The CGL policy also usually excludes liability for intentional acts such as:

- (1) Breach of contract, other than misappropriation of advertising ideas under an implied contract;
- (2) The failure of goods, products or services to conform with advertised quality or performance;
- (3) The wrong description of the price of goods, products or services;
- (4) An offense committed by an insured whose business is advertising, broadcasting, publishing or telecasting.<sup>41</sup>

Some policies specifically *exclude* patent infringement by defining "advertising injury" as "injury occurring in the course of the named insured's advertising activities, if such injury arises out of libel, slander, defamation, violation of right of privacy, piracy, unfair competition, or infringement of a copyright, title or slogan (*other than a patent*)."<sup>42</sup>

### C. *Interpreting an Insurance Policy*

#### 1. *Interpreting the Coverage Provided by the Policy*

State law governs the substantive issues in an insurance coverage lawsuit.<sup>43</sup> Generally, CGL policies are adhesion contracts.<sup>44</sup> An adhesion contract is one in which one party to the contract can bargain regarding the amount, limits, and coverage of insurance, but not the definitions and conditions.<sup>45</sup>

Even if the insured is a large corporation with substantial annual sales, it procures the coverage through an insurance broker, and it is able to bargain on relatively equal terms with

40. *Aetna Casualty & Sur. Co. v. Centennial Ins. Co.*, 838 F.2d 346, 348 (9th Cir. 1988).

41. *Tobin & Myslis*, *supra* note 37.

42. *Aetna Casualty & Sur. Co.*, 838 F.2d at 349 (emphasis added).

43. Although California law is used as an example in this article, the substantive law in other states governing the interpretation of insurance contracts is similar.

44. *Clemco Indus. v. Commercial Union Ins. Co.*, 665 F. Supp. 816, 818 (N.D. Cal. 1987), *aff'd*, 848 F.2d 1242 (9th Cir. 1988).

45. *Id.*

the insurance company concerning issuance of the policy, the insurance contract may still be an adhesion contract.<sup>46</sup> The most significant issue in determining whether a contract is an adhesion contract is whether the insured had participated in drafting the terms, language and/or options offered in the insurance policy.<sup>47</sup>

In interpreting an insurance policy, consideration must be given to the intent of the parties and the reasonable expectations of the insured.<sup>48</sup> The policy language is the best evidence of the intent of the parties.<sup>49</sup>

The words used in an insurance contract must be given their plain meaning, the meaning "a lay person would normally attach to them."<sup>50</sup> If the dictionary definitions of an ambiguous term provide a range of reasonable meanings, the court "must apply the meaning which provides the most coverage for the insured."<sup>51</sup> "In construing the language of an insurance policy, the court should give the words their plain and ordinary meaning, unless the policy clearly indicates to the contrary."<sup>52</sup>

The primary purpose of an insurance policy is to pay damages which the insured becomes legally obligated to pay. This is referred to as "indemnity." An insurance liability policy should be interpreted to provide coverage and indemnification whenever possible.<sup>53</sup> However, if the insurer has limited coverage of risks in the policy, the "plain language of that limitation must be observed."<sup>54</sup> These limitations must be clearly stated so the insured is aware of the effect of the exceptions.<sup>55</sup> "[A]n insurer cannot avoid its primary duty to provide coverage by incorporating into an insurance policy an exclusionary

---

46. *Id.* at 819.

47. *Id.*

48. *Insurance Co. of N. Am. v. Gibalco, Inc.*, 847 F.2d 530, 534 (9th Cir. 1988); *see also Continental Casualty Co. v. City of Richmond*, 763 F.2d 1076, 1079 (9th Cir. 1985) (similar language).

49. *City of Richmond*, 763 F.2d at 1080.

50. *Poland v. Martin*, 761 F.2d 546, 548 (9th Cir. 1985).

51. *Id.*

52. *St. Paul Mercury Ins. Co. v. Medical Laboratory Network, Inc.*, 690 F. Supp. 901, 903 (C.D. Cal. 1988).

53. *Hancock Laboratories, Inc. v. Admiral Ins. Co.*, 777 F.2d 520, 524 (9th Cir. 1985).

54. *Wagner v. Federal Emergency Management Agency*, 847 F.2d 515, 522 (9th Cir. 1988).

55. *Continental Casualty Co. v. City of Richmond*, 763 F.2d 1076, 1079 (9th Cir. 1985).

policy clause that is ambiguous.”<sup>56</sup> Coverage clauses are interpreted broadly so that the insured receives the greatest possible protection, but exclusionary clauses are construed narrowly against the insurer.<sup>57</sup>

It is well settled that ambiguities in insurance contracts are construed against the insurer.<sup>58</sup> Although a court should not “strain for interpretations to create ambiguities where none exist,” where an ambiguity does exist, it should be interpreted in favor of coverage, particularly if the ambiguity is in an exclusionary clause.<sup>59</sup> If more than one interpretation is reasonable, the court must adopt the interpretation that favors coverage.<sup>60</sup> If two different risks cause a loss and each is of independent origin, one of which is excluded under the policy and one of which is not excluded, the loss is covered.<sup>61</sup>

Cases requiring interpretation of insurance contracts raise questions of law and, thus, are particularly amenable to summary judgment.<sup>62</sup> “[I]n ruling on a motion for summary judgment, the judge must view the evidence presented through the prism of the substantive evidentiary burden.”<sup>63</sup> There is no issue for trial unless there is sufficient evidence favoring the non-moving party for a jury to return a verdict for that party.<sup>64</sup>

## 2. *Interpreting the Duty to Defend*

In addition to providing indemnity, a CGL policy provides that the insurer will assume the defense of any claims which are covered by the policy. “[T]he duty to defend is broad and insurance policies must be interpreted so as to protect the reasonable expectations of the insured.”<sup>65</sup> Uncertainty as to whether the duty to defend exists is resolved in favor of the

---

56. *Interstate Fire & Casualty Co. v. Stuntman, Inc.*, 861 F.2d 203, 204 (9th Cir. 1988).

57. *City of Richmond*, 763 F.2d at 1079.

58. *Insurance Co. of N. Am. v. Gibrasco, Inc.*, 847 F.2d 530, 534 (9th Cir. 1988).

59. *Poland v. Martin*, 761 F.2d 546, 548 (9th Cir. 1985) (citations omitted).

60. *Gibrasco, Inc.*, 847 F.2d at 534.

61. *Poland*, 761 F.2d at 549.

62. See, e.g., *Iowa Kemper Ins. Co. v. Stone*, 269 N.W.2d 885 (Minn. 1978); *State Farm Mutual Auto Ins. Co. v. Budget Rent-A-Car Sys., Inc.*, 359 N.W.2d, 673 (Minn. Ct. App. 1984).

63. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 254 (1986).

64. *Id.* at 257.

65. *St. Paul Mercury Ins. Co. v. Medical Laboratory Network*, 690 F. Supp. 901, 903 (C.D. Cal. 1988).

insured.<sup>66</sup>

When the language of the policy is clear, the court must not give it a strained construction to impose on the insurer a liability it has not assumed. Where the scope of the basic coverage itself is at issue, the insured has the burden of showing that the event is a claim within the scope of the basic coverage. If there is no potential for coverage, the insurer has no duty to defend.<sup>67</sup>

The complaint against the insured need only allege facts which give rise to potential liability under the policy to trigger the insurer's duty to defend.<sup>68</sup> "An insurance company 'bears a duty to defend its insured whenever it ascertains facts which give rise to the potential of liability under the policy.'"<sup>69</sup> When an insurer learns of facts that create potential liability, the insurer must furnish a defense.<sup>70</sup>

"An insurer's duty to defend must be analyzed and determined on the basis of any potential liability arising from the facts available to the insurer from the complaint or other sources available to it at the time of the tender of defense."<sup>71</sup> The duty to defend is broader than the duty to indemnify, and requires the insurer to investigate and evaluate the facts expressed or implied in the complaint as well as those learned from other sources.<sup>72</sup>

The insurer's obligation to defend is not dependent on the facts contained in the complaint alone; the insurer must furnish a defense when it learns of facts from *any* source that creates [sic] a potential of liability under its policy. Indeed, the duty to defend is so broad that as long as the complaint contains language creating the potential of liability under an insurance policy, the insurer must defend an action

---

66. *Aetna Casualty & Sur. Co. v. Centennial Ins. Co.*, 838 F.2d 346, 350 (9th Cir. 1988).

67. *Hartford Fire Ins. Co. v. Karavan Enters., Inc.*, 659 F. Supp. 1075, 1076 (N.D. Cal. 1986) (citations omitted).

68. *Previews, Inc. v. California Union Ins. Co.*, 640 F.2d 1026, 1027 (9th Cir. 1981).

69. *Isaacson v. California Ins. Guar. Ass'n*, 44 Cal. 3d 775, 792, 750 P.2d 297, 308, 244 Cal. Rptr. 655, 666 (1988) (quoting *Gray v. Zurich Ins. Co.*, 65 Cal. 2d 263, 276-77, 419 P.2d 168, 177, 54 Cal. Rptr. 104, 113 (1966)).

70. *Lassen Canyon Nursery, Inc. v. Royal Ins. Co. of Am.*, 720 F.2d 1016, 1017 (9th Cir. 1983).

71. *Aetna Casualty & Sur. Co. v. Centennial Ins. Co.*, 838 F.2d 346, 350 (9th Cir. 1988).

72. *Hartford Fire Ins. Co. v. Karavan Enters., Inc.*, 659 F. Supp. 1075, 1076 (N.D. Cal. 1986).

against its insured even though it has independent knowledge of facts not in the pleadings that establish that the claim is *not* covered.<sup>73</sup>

If the potential for liability is “tenuous and farfetched,” however, the insurer will not be required to defend its insured.<sup>74</sup> “The duty to defend a suit which raises a *possibility* of liability, but is eventually shown to be groundless, does not equate with a duty to defend a suit which raises *no* potential liability.”<sup>75</sup>

The insurer’s obligation, however, is not unlimited. It is limited first by the language of the insurance contract itself. As discussed above, the parties may specifically agree as to whether certain events are covered through the use of exclusions. “When the language of the policy is clear, the court must not give it a strained construction to impose on the insurer a liability it has not assumed.”<sup>76</sup> An insurer bears the burden of proving the applicability of an exclusion.<sup>77</sup>

[A]n insurer’s implied duty to defend may not be waived absent an explicit provision to that effect: “[T]he law imposes an implied obligation to defend where it is not expressly and clearly omitted from the particular risk. . . . [I]f the exclusion is unclear or uncertain and is reasonably to be expected by the insured the obligation will be implied by law and included as part of the agreement.”<sup>78</sup>

Furthermore, [w]rongful failure to provide coverage or defend a claim is a breach of contract. Accordingly, if an insurer “erroneously denies coverage and/or improperly refuses to defend the insured” in violation of its contractual duties, “the insured is entitled to make a reasonable settlement of the claim in good faith and may then maintain an action against the insurer to recover the amount of the settlement.”<sup>79</sup>

---

73. *Aetna Casualty & Sur. Co.*, 838 F.2d at 350 (emphasis by the court) (citations omitted).

74. *Lassen Canyon Nursery, Inc.*, 720 F.2d at 1018.

75. *Aetna Casualty & Sur. Co.*, 838 F.2d at 350.

76. *Karavan Enters., Inc.*, 659 F. Supp. at 1076.

77. *State Farm Fire & Casualty Co. v. Martin*, 872 F.2d 319, 321 (9th Cir. 1989).

78. *Interstate Fire & Casualty Co. v. Stuntman, Inc.*, 861 F.2d 203, 205 (9th Cir. 1988) (quoting *Aetna Casualty & Sur. Co. v. Certain Underwriters*, 56 Cal. App. 3d 791, 799, 129 Cal. Rptr. 47, 53 (1976)).

79. *Isaacson v. California Ins. Guar. Ass’n*, 44 Cal. 3d 775, 791, 750 P.2d 297, 308, 244 Cal. Rptr. 655, 666 (1988) (quoting *Clark v. Bellefonte Ins. Co.*, 113 Cal. App. 3d 326, 335, 169 Cal. Rptr. 832, 832 (1980) (citations omitted)).

### 3. *The Duty to Provide Independent Counsel*

The insured and the insurer may disagree as to whether a certain claim falls within the scope of coverage of the policy. In *San Diego Navy Federal Credit Union v. Cumis Insurance Society, Inc.*,<sup>80</sup> the California Court of Appeals held that an insured has the right to select independent counsel paid for by the insurer where an actual or potential conflict has arisen between the insured and the insurer.<sup>81</sup> "It is now beyond question that under certain circumstances an insurer is obligated to pay for 'independent' counsel chosen by the insured."<sup>82</sup>

The court of appeals quoted, in *Cumis Insurance Society*, a 1984 California Court of Appeals decision to support this proposition:

It has long been the law in this state that when a conflict develops, the *insurer* cannot compel the insured to surrender control of the litigation, and must, if necessary, secure independent counsel for the insured. . . . [T]he insurer's obligation [to defend, after the appearance of a conflict], "extends to paying the reasonable value of the legal services and costs performed by independent counsel selected by the insured."<sup>83</sup>

This concept has been codified in section 2860 of the California Civil Code.<sup>84</sup>

When a question exists as to whether an occurrence is covered by the insurance policy, independent counsel representing the insured's interest is required. The insurer is contractually obligated to pay for the insured's independent counsel.<sup>85</sup> Once the insurer decides to assert a coverage defense, the same attorney may not represent both the insured and the insurer.<sup>86</sup> If the insured and the insurer are repre-

---

80. 162 Cal. App. 3d 358, 208 Cal. Rptr. 494 (1984).

81. *Id.* at 361, 208 Cal. Rptr. at 496.

82. *Employers Ins. of Wausau v. Albert D. Seeno Constr. Co.*, 692 F. Supp. 1150, 1154 (N.D. Cal. 1988).

83. *Purdy v. Pacific Auto. Ins. Co.*, 157 Cal. App. 3d 59, 76-77, 203 Cal. Rptr. 524, 534 (1984) (quoting *Previews, Inc. v. California Union Ins. Co.*, 640 F.2d 1026, 1028 (9th Cir. 1981)), *quoted in Cumis Ins. Soc., Inc.*, 162 Cal. App. 3d at 364 n.3, 208 Cal. Rptr. at 498 n.3.

84. CAL. CIVIL CODE § 2860 (West Supp. 1991); *Employers Ins. of Wausau*, 692 F. Supp. at 1155. For a discussion of California's codification of the duty to defend, see *id.* at 1155-58.

85. *Cumis Ins. Soc., Inc.*, 162 Cal. App. 3d at 364, 208 Cal. Rptr. at 497-98.

86. *Id.* at 364, 208 Cal. Rptr. at 498.

sented by two different attorneys, each of whom is pledged to promote and protect the prime interests of his client, adequate representation is guaranteed. This averts the deleterious effect of the conflict of interest imposed on an attorney who attempts the difficult task of representing both parties.<sup>87</sup>

## II. ANALYSIS

### A. Early Attempts to Obtain Coverage

*John Deere Insurance Co. v. Shamrock Industries, Inc.*<sup>88</sup> discusses the issue of insurance coverage in the context of intellectual property. Shamrock Industries commenced an action against several defendants alleging patent infringement, misappropriation of trade secrets, unfair competition and breach of contract.<sup>89</sup> One defendant (Metal Craft) tendered the defense of the underlying action to its insurer (Deere), claiming that a number of insurance policies it had purchased obligated its insurer to defend the action.<sup>90</sup> Deere refused to tender the defense and subsequently commenced a declaratory judgment action requesting that the court decide whether it had a duty to defend or indemnify the defendants in this action<sup>91</sup>

Six different insurance policies were at issue in *Shamrock*, all of which required Deere to defend the insured against suits alleging "advertising injury." Deere and the defendants vigorously disputed the meaning of that phrase. The policies all defined "advertising injury" in essentially the same fashion.<sup>92</sup> Deere contended that "the suit brought by Shamrock clearly falls outside of the[ ] definitions of advertising injury."<sup>93</sup>

The district court acknowledged that "[v]ery little legal au-

---

87. *Id.* at 365 n.4, 208 Cal. Rptr. at 498 n.4.

88. 696 F. Supp. 434 (D. Minn. 1988), *aff'd*, 929 F.2d 413 (8th Cir. 1991).

89. *Id.* at 435.

90. *Id.*

91. *Id.* The declaratory judgment action required the court to examine five different areas of the policies:

- (1) the scope of the word "insureds";
- (2) the phrase "advertising injury";
- (3) the meaning of exclusion of all advertising activity coverage where the first publication occurred prior to the commencement of the policy period;
- (4) the meaning of the phrase "actual malice"; and
- (5) the meaning of a provision excluding liability "assumed by the insured under any contract or agreement."

*Id.* at 436.

92. See *supra* notes 35-39 and accompanying text.

93. *Shamrock Indus., Inc.*, 696 F. Supp. at 437.



thority exists to provide guidance in interpreting the precise meaning of the phrase 'advertising activity.'"<sup>94</sup> It noted that the Minnesota Supreme Court's definition of "advertising activity" ("public or widespread distribution of the alleged [advertising] material") relied on by Deere was "rather narrow[ ]" and "not entirely applicable."<sup>95</sup> The court compared that definition with the "broad" dictionary definition of "advertise" ("[a]ny oral, written, or graphic statement made by the seller in any manner in connection with the solicitation of business . . .").<sup>96</sup>

The court concluded that "[t]he Minnesota Supreme Court's interpretation was grounded in part on 'companion words found in the exclusion.'"<sup>97</sup> "Those companion words were 'broadcasting' and 'telecasting,' which tend to indicate more widespread distribution."<sup>98</sup> There were no such companion words in the insurance policies at issue in the *Shamrock* case, and the court concluded that the state supreme court interpretation was not controlling.<sup>99</sup>

Relying on the specific "advertising" acts of the insured, the court found that "the claims for misappropriation of trade secrets alleged arguably fall within the coverage of the appropriate policy."<sup>100</sup> The court's decision was based on one of the defendants having sent three letters to a potential buyer proclaiming the strengths and virtues of the accused device.<sup>101</sup> According to the court, these letters "arguably constituted advertising activity."<sup>102</sup>

The insurer argued that, even if the letters and demonstra-

---

94. *Id.* at 439.

95. *Id.* (quoting *Fox Chem. Co. v. Great Am. Ins. Co.*, 264 N.W.2d 385, 386 (Minn. 1978)).

96. *Id.* (quoting BLACK'S LAW DICTIONARY 50 (5th ed. 1979)).

97. *Id.* (quoting *Fox Chemical Co.*, 264 N.W.2d at 386).

98. *Id.*

99. *Id.*

100. *Id.* at 440.

101. *Id.*

The first letter, dated November 1, 1985, stated, "We can build machines to help you sell more containers." The second letter, dated January 20, 1986, stated such things as "we will warrant each unit for one year. We also furnish a complete maintenance manual with each machine." The third letter, written on approximately March 1, 1986, listed the machine's "selling points" and enclosed pictures.

*Id.* (footnote omitted). Further, demonstrations of the machine were held on the premises for some potential customers. *Id.*

102. *Id.*

tions were considered "advertising activity," it had no duty to defend since the "policies still require that one of the offenses stated in the policies arise out of that activity and be complained of in the underlying action."<sup>103</sup> Deere contended that "the allegations in the Complaint . . . did not arise out of the sending of the letters or conducting of the demonstrations, but rather arose from the totally unrelated infringement of Shamrock's patent rights."<sup>104</sup>

The defendants responded:

[T]he claims of misappropriation of trade secrets and unfair competition do arise out of the advertising activity because, but for that activity, there would not have been a disclosure of trade secret information, an essential element of a misappropriation of the trade secret claim. Defendants further argued that neither the language of the insurance policies nor case law require there to be a proximate cause between the advertising activity and the injury alleged for that injury to "arise out of the advertising activity."<sup>105</sup>

The court agreed with the defendants because "the underlying claims need only *arguably* fall within the coverage of the policies and because any reasonable differing interpretation [of the policies] must be construed against the insurer."<sup>106</sup> Consequently, the "misappropriation of trade secrets" claim was covered by the CGL policy and, since part of the cause of action is arguably within the scope of coverage, the insurer had the duty to defend all claims, including the patent infringement claim.<sup>107</sup>

In *National Union Fire Insurance Co. of Pittsburgh, Pa. v. Siliconix Inc.*,<sup>108</sup> the court directly addressed the narrower issue of whether patent infringement, pleaded alone, is covered by an insurance policy as "advertising injury." The initial question

---

103. *Id.* There is some confusion in the case law concerning the specific language of the policy applicable to this issue. Some courts, such as the court in *Shamrock*, discuss the injury "arising out of" the advertising activity. Other courts discuss injuries arising "in the course of" advertising activities. *See, e.g.*, *National Union Fire Ins. Co. of Pittsburgh, Pa. v. Siliconix, Inc.*, 729 F. Supp. 77 (N.D. Cal. 1989). Regardless of the specific language in the policies, the issue is identical: whether there is sufficient causality between the advertising activities and the underlying action (*e.g.*, patent infringement) to bring the coverage into effect.

104. *Shamrock Indus., Inc.*, 696 F. Supp. at 440.

105. *Id.*

106. *Id.* (emphasis added).

107. *Id.*

108. 729 F. Supp. 77 (N.D. Cal. 1989).

before the court was whether the term "piracy," as used in the policy, encompasses patent infringement.<sup>109</sup> The court held that the term "piracy" is "ambiguous and is capable of at least two definitions, . . . one encompassing patent infringement and one not."<sup>110</sup> "Read in its ordinary sense, it must be found to include patent infringement."<sup>111</sup> Since the term was "susceptible to two reasonable interpretations," the court construed it in favor of coverage for the insured.<sup>112</sup> Consequently, the court found that the term "piracy" includes patent infringement.<sup>113</sup> The court did not reach the question of whether "patent infringement" is encompassed by the term "unfair competition."<sup>114</sup>

The court next addressed whether the injury arising out of patent infringement "occurred in the course of" advertising activities.<sup>115</sup> The court first noted that, to infringe a patent, one must make, use, or sell the patented invention, not merely advertise the patented invention.<sup>116</sup> Siliconix argued that "advertising is part and parcel of selling, and therefore the selling of an infringing product is an infringement occurring in the course of advertising."<sup>117</sup>

The court found that Siliconix's argument "contains a fundamental flaw in that it reads the requirement that the infringement occur in the course of advertising" too broadly and "beyond the reasonable expectations of the insured."<sup>118</sup>

Taken to its extreme, this argument would lead to the conclusion that any harmful act, if it were advertised in some way, would fall under the grant of coverage merely because it was advertised. Under this rationale, for instance, injury due to a defective product which is sold as a result of advertising activity and which later harms a consumer, may fall within the coverage grant.<sup>119</sup>

Consequently, the court found that "even if piracy is construed

---

109. *Id.* at 79.

110. *Id.*

111. *Id.*

112. *Id.*

113. *Id.*

114. *Id.* at 79 n.2.

115. *Id.* at 79.

116. *Id.*

117. *Id.*

118. *Id.* at 80.

119. *Id.*

to encompass patent infringement, patent infringement does not occur in the course of advertising, and is not covered as a type of advertising injury.”<sup>120</sup>

The court believed that it was essentially “faced with a choice between giving meaning to the term ‘piracy’ or giving meaning to the clause ‘occurring in the course of the named insured’s advertising activities.’”<sup>121</sup> The court noted its awareness of “the need to protect the insured’s reasonable expectations of coverage and that the insured could have excluded patent infringement from its coverage by expressly stating that ‘piracy’ does not include patent infringement.”<sup>122</sup> However, the court was also “aware of the requirement that insurance contracts be read as a whole and that each clause be given meaning whenever possible. In light of this requirement, the Court [could not] nullify the clause requiring that the injury occur in the course of advertising.”<sup>123</sup>

### B. *The Intex Case*

In *Intex Plastics Sales Co. v. United National Insurance Co.*,<sup>124</sup> Intex was charged with directly infringing U.S. Patent No. 3,585,356, as well as actively inducing infringement of that patent and contributorily infringing that patent.<sup>125</sup> Two insurers, First State and New England, agreed to provide a defense to Intex, subject to a reservation of rights, but the third insurer, United, declined to tender a defense.<sup>126</sup>

The court granted Intex’s motion for summary judgment as to coverage.<sup>127</sup> It noted that “[w]hether language in an insurance contract is ambiguous is a question of law”<sup>128</sup> and that “[a]mbiguities are construed against the insurer-draftsman to protect the insured’s reasonable expectations of coverage.”<sup>129</sup>

The policy at issue in *Intex* defined “Advertising Injury” as “injury arising out of an offense committed during the policy

---

120. *Id.*

121. *Id.* at 81.

122. *Id.*

123. *Id.*

124. 18 U.S.P.Q.2d (BNA) 1567 (C.D. Cal. Dec. 6, 1990).

125. *Id.* at 1568.

126. *Id.* at 1568-69.

127. *Id.* at 1570.

128. *Id.* at 1569.

129. *Id.* (citing *Siliconix, Inc.*, 729 F. Supp. at 79).

period occurring in the course of the named insured's advertising activities, if such injury arises out of libel, slander, defamation, violation of right of privacy, piracy, unfair competition, or infringement of copyright, title or slogan."<sup>130</sup> The terms "advertising activities," "piracy" and "unfair competition" were not defined in the policy.<sup>131</sup> The court held that a patent infringement suit is covered as "advertising injury" under a CGL policy.<sup>132</sup>

Construing the term "piracy" against the insurer, the court concluded that "piracy" includes patent infringement.<sup>133</sup> It also concluded that patent infringement is "unfair competition" because it "is an unfair business practice, is anti-competitive and is prohibited by law."<sup>134</sup> The latter determination was made after reviewing California common law ("unfair competition means any unfair business prohibited by law")<sup>135</sup> and a California statute ("unfair competition 'shall mean and include unlawful, unfair or fraudulent business practice and unfair, deceptive, untrue or misleading advertising' ").<sup>136</sup>

Noting that the duty to defend arises so long as there is the "possibility" or "potential" for liability under the policy, the court held that the insurers have a duty to defend.<sup>137</sup> The court also noted that the insurers failed to show that infringement by Intex was "willful" or that the "loss-in-progress" rule applied.<sup>138</sup>

### C. Applying Intex

#### 1. Does Patent Infringement "Arise" from Advertising Activity?

The most troubling aspect of *Intex* is its failure to address the issue of whether patent infringement "arose" out of the in-

---

130. *Id.* at 1568.

131. *Id.*

132. *Id.* at 1569.

133. *Id.* (citing *Graver Tank Co. v. Linde Air Prods. Co.*, 339 U.S. 605 (1950)).

134. *Id.*

135. *Id.* (citing *People v. McKale*, 25 Cal. 3d 626, 631-32, 159 Cal. Rptr. 81 (1979)).

136. *Id.* (quoting Cal. Bus. & Prof. Code § 17200).

137. *Id.* at 1569-70.

138. *Id.* at 1570. The "loss-in-progress" rule states that an insurer may insure only against contingent or unknown risks. Therefore, liability will not be imposed under an insurance policy where damages occur and are apparent before the date the policy takes affect. *Home Ins. Co. v. Landmark Ins. Co.*, 205 Cal. App. 3d 1388, 1395, 253 Cal. Rptr. 277, 282 (1988).

sured's advertising activities or "occurred in the course of" those activities. The *Siliconix* court found that the term "piracy" encompassed patent infringement, but that the patent infringement did not "occur in the course of" those advertising activities.<sup>139</sup> However, in *Shamrock*, the court held that the disclosure of trade secrets "arose" from advertising activities.<sup>140</sup> If *Shamrock* had not involved a trade secrets action, and instead had involved only a patent infringement action, would the result have been the same? If *Intex* had addressed this issue, would the result have been different?

The phrase "arising out of" carries much broader significance than "caused by." It is ordinarily understood to mean "'originating from,' 'having its origin in,' 'growing out of,' or 'flowing from,' or, in short, 'incident to, or having connection with.'"<sup>141</sup> Courts have consistently adopted broad definitions of "arising from" and "arising out of."<sup>142</sup>

Similarly, the term "arising out of the insured's advertising activities" should be given a broad definition. Typically, the term "arising out of" is found in insurance policy exclusions. Despite the fact that policy exclusions are construed narrowly, the term "arising out of" has been broadly interpreted. For example, a malpractice action against a psychologist who had sex with a patient "arose out of" sexual acts performed by the insured;<sup>143</sup> a negligence action against a wife whose husband molested children at their nursery school "arose out of" the operation of the nursery school;<sup>144</sup> a personal injury claim against a coal operator "arose out of" pollution discharge over a seven to eight year period;<sup>145</sup> and a wrongful death claim for a security guard killed by a fellow security guard "arose out of" his employment.<sup>146</sup>

Some courts apply a "but for" analysis in analyzing whether

---

139. For a discussion of the term "piracy," see *supra* text accompanying notes 109-13.

140. See *supra* notes 100-07 and accompanying text.

141. *Continental Casualty Co. v. City of Richmond*, 763 F.2d 1076, 1080 (9th Cir. 1985) (quoting *Red Ball Motor Freight, Inc. v. Employers Mut. Liab. Ins. Co.*, 189 F.2d 374, 378 (5th Cir. 1951)).

142. *Id.*

143. *Govar v. Chicago Ins. Co.*, 879 F.2d 1581, 1582-83 (8th Cir. 1989).

144. *American States Ins. Co. v. Borbor*, 826 F.2d 888, 891-93 (9th Cir. 1987).

145. *United States Fidelity & Guar. Co. v. Star Fire Coals, Inc.*, 856 F.2d 31, 33-34 (6th Cir. 1988).

146. *Forum Ins. Co. v. Allied Sec., Inc.*, 866 F.2d 80, 83 (3d Cir. 1989).

liability arose from certain conduct. For example, in *Arndt v. American Family Insurance Co.*,<sup>147</sup> the Minnesota Supreme Court held that a personal injury action for injuries incurred while using a chopper box arose out of the ownership, use and control of some uninsured property. The insured and a friend were using the chopper box to chop cornstalks to be used as bedding in a barn.<sup>148</sup> The barn was uninsured.<sup>149</sup> The insured's friend was injured and sued for his personal injury.<sup>150</sup> The insurer refused to indemnify the insured under his "Farm Family Liability Policy" because the policy excluded liability for acts "arising out of the ownership, use or control by or rental to any insured of any premises, other than the insured premises."<sup>151</sup>

The court agreed with the insurer. Focusing on whether there was a "causal relationship" between the insured's liability and the excluded (uninsured) premises, the court found that the defendant "would not have been negligently using the chopper box on New Year's Day *but for* his desire to provide bedding for the barn."<sup>152</sup> In other words, recovery requires a "causal nexus" between the liability and the act from which it arises.<sup>153</sup>

At least one court has addressed the related question concerning the breadth of "advertising activity." In *Playboy Enterprises v. St. Paul Fire & Marine Insurance Co.*,<sup>154</sup> Playboy was sued by Penthouse for libel and various business torts.<sup>155</sup> The action was based on a letter that one of Playboy's regional advertising managers had sent to eleven advertisers.<sup>156</sup> The letter erroneously stated that Penthouse had failed to meet its circulation guarantees by not selling the number of magazines that it claimed to have sold.<sup>157</sup> Playboy tendered the defense to its

---

147. 394 N.W.2d 791 (Minn. 1986).

148. *Id.* at 792.

149. *Id.* at 793.

150. *Id.* at 792.

151. *Id.* at 794.

152. *Id.* at 795 (emphasis added).

153. *Id.* (citing *St. Paul Fire & Marine Ins. Co. v. Insurance Co. of N. Am.*, 501 F. Supp. 136, 139 (W.D. Va. 1980)).

154. 769 F.2d 425 (7th Cir. 1985).

155. *Id.* at 427.

156. *Id.*

157. *Id.*

insurance company and the tender was refused.<sup>158</sup> After its insurer refused to defend, Playboy retained its own counsel and incurred over \$400,000 in attorneys fees and costs.<sup>159</sup> The court subsequently dismissed the libel action.<sup>160</sup>

Playboy filed a complaint against St. Paul Fire & Marine Insurance Company (St. Paul) for breach of the insurance contract, claiming that St. Paul should have defended Playboy against the libel action and that St. Paul should reimburse Playboy for attorneys fees incurred in defending the libel case.<sup>161</sup> The district court granted Playboy's motion for summary judgment, holding that distribution of the eleven letters by the Playboy employee was not excluded from the policy's coverage because such distribution did not constitute advertising.<sup>162</sup>

On appeal, St. Paul argued that the district court's decision should be reversed since the insurance policy "did not cover suits relating to the defamatory material that Playboy had disseminated."<sup>163</sup> The issue before the appellate court was whether the eleven letters sent out by Playboy to advertisers and advertising agencies referring to Penthouse's failure to meet circulation guarantees constituted publications or utterances "in the course of or related to advertising, broadcasting or telecasting activities conducted by or on behalf of the Named Insured" under the policy's exclusionary provision.<sup>164</sup>

The court relied on *Webster's Dictionary* in defining "advertising" as "the action of calling something (as a commodity for sale, a service offered or desired) to the attention of the public especially by means of printed or broadcast paid announcements."<sup>165</sup> "This definition requires the presentation of the item to be sold or approved be made in a medium directed to the public at large."<sup>166</sup> The court noted with approval that this interpretation of the term "advertising" to mean public or widespread distribution had already been adopted by the Min-

---

158. *Id.*

159. *Id.*

160. *Id.*

161. *Id.*

162. *Id.* The court awarded Playboy \$395,459.95—\$287,385.23 in costs and \$108,074.72 in prejudgment interest.

163. *Id.*

164. *Id.* at 428.

165. *Id.* (quoting WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY OF THE ENGLISH LANGUAGE 31 (unabridged ed. 1963)).

166. *Id.*



nesota Supreme Court.<sup>167</sup>

The exclusionary provision in the insurance policy excluded coverage for any publication or utterance "in the course of or related to advertising."<sup>168</sup> The court agreed that Playboy's "dissemination of the eleven letters, while not advertising per se, was related to an activity designed to promote one of Playboy's products, advertising space, to potential buyers of the space and thus appears to come within the plain meaning of the clause 'related to advertising activities.'"<sup>169</sup>

Similar broad definitions of "arising out of" and "advertising activity" should apply to patent infringement. The definition of advertising used in *Playboy* emphasizes the purpose of advertising—to sell a product.<sup>170</sup> Sale of an infringing article subjects the seller to liability for patent infringement.<sup>171</sup> Since there would be no sale "but for" the advertising, the sale "arises out of" the advertising activity.

The court in *Siliconix*<sup>172</sup> rejected a similar argument. "Taken to its extreme," that court reasoned, "this argument would lead to the conclusion that any harmful act, if it were advertised in some way, would fall under the grant of coverage merely because it was advertised."<sup>173</sup> For example, the *Siliconix* court explained, "injury due to a defective product which is sold as a result of advertising activity and which later harms a consumer, may fall within the coverage grant."<sup>174</sup>

However, this analogy is inapposite. In a patent infringement action, liability results from the sale of an infringing product.<sup>175</sup> In a products liability action, liability does not exist because the product was sold; it exists because the product is defective.<sup>176</sup> The sale of the product, and the related adver-

---

167. *Id.* at 428-29 (citing *Fox Chem. Co. v. Great Am. Ins. Co.*, 264 N.W.2d 385, 386 (Minn. 1978)).

168. *Id.* at 429.

169. *Id.*

170. See *supra* text accompanying note 165.

171. "Except as otherwise provided in this title, whoever without authority makes, uses or sells any patented invention, within the United States during the term of the patent therefor, infringes the patent." 35 U.S.C. § 271(a) (1988).

172. *National Union Fire Insurance Co. of Pittsburgh, Pa. v. Siliconix Inc.*, 729 F. Supp. 77 (N.D. Cal. 1989).

173. *Id.* at 80.

174. *Id.*

175. See *supra* note 171.

176. See RESTATEMENT (SECOND) OF TORTS § 402A (1965).

tising of the product, are not essential for liability. In the context of a patent infringement suit, "but for" the sale of an infringing product, there is no patent infringement and, "but for" the advertising, there would be no sale. In the context of a products liability suit, without the advertising and sale of a defective product, there is still a cause of action for products liability.

Therefore, the sale of an infringing article as a result of advertisements or other solicitations "arises out of" the infringer's advertising activities. In the situation in which the infringing article is sold through advertisements, coverage for patent infringement exists under a CGL policy.

## 2. Is Patent Infringement "Unfair Competition"?

The courts in both *Siliconix* and *Intex* agree that the term "piracy" in a CGL policy covers patent infringement.<sup>177</sup> However, many policies do not contain this term. *Intex* also held that the CGL policy covers acts of patent infringement under the broader term "unfair competition."<sup>178</sup> Is patent infringement "unfair competition"?

"Unfair competition" is a broad common law business tort.<sup>179</sup> Courts have noted "an 'incalculable variety' of illegal practices falling under the unfair competition rubric. . . . The tort is adaptable and capacious."<sup>180</sup> Usually, unfair competition consists of the "taking and use of plaintiff's property to compete against the plaintiff's own use of the same

177. This conclusion is based on a sentence from *Graver Tank & Mfg. Co. v. Linde Air Prods. Co.*, 339 U.S. 605 (1950), more famous for its elucidation of the doctrine of equivalents: "One who seeks to pirate an invention, like one who seeks to pirate a copyrighted book or play, may be expected to introduce minor variations to conceal and shelter the piracy." *Id.* at 607.

178. *Intex Plastics Sales Co. v. United National Insurance Co.*, 18 U.S.P.Q.2d (BNA) 1567, 1569 (C.D. Cal. Dec. 6, 1990). The *Siliconix* court specifically stated that it did not reach the issue of whether patent infringement is "unfair competition" under a CGL policy. *Siliconix, Inc.*, 729 F. Supp. at 79 n.2.

179. *International Order of Job's Daughters v. Lindeburg & Co.*, 633 F.2d 912, 915 (9th Cir. 1981).

180. *Roy Export Co. Establishment of Vaduz, Liechtenstein v. Columbia Broadcasting Sys.*, 672 F.2d 1095, 1105 (2d Cir. 1982) (citing *Ronson Art Metal Works, Inc. v. Gibson Lighter Mfg. Co.*, 3 A.D.2d 227, 230-31, 159 N.Y.S.2d 606, 609-10 (1957)). The *Ronson* court recognized that "[t]he incalculable variety of illegal commercial practices denominated as unfair competition is proportionate to the unlimited ingenuity that overreaching entrepreneurs and trade pirates put to use." *Ronson Art Metal Works, Inc.*, 3 A.D.2d at 230-31, 159 N.Y.S.2d at 609-10.

property.”<sup>181</sup>

The doctrine of unfair competition is broad and flexible,<sup>182</sup> and has been described as “encompassing ‘any form of commercial immorality.’”<sup>183</sup> It is “endeavoring to reap where [one] has not sown”<sup>184</sup> by taking “the skill, expenditures and labor of a competitor”<sup>185</sup> or “misappropriat[ing] for the commercial advantage of one person . . . a benefit of ‘property’ right belonging to another.”<sup>186</sup> However, the “essence of an unfair competition claim . . . is that the defendant has misappropriated the labors and expenditures of another.”<sup>187</sup> A claim of unfair competition is actionable only to vindicate a legally protected property interest.<sup>188</sup>

A patent is a legally protected property interest.<sup>189</sup> A patent infringer takes the skill, expenditures and labor of a competitor and misappropriates the benefit of a property right belonging to another. Patent infringement consists of taking and using plaintiff’s property (the patent) to compete against the plaintiff’s own use of the same property by selling infringing products.

Just as trademark infringement is a specific species of unfair competition,<sup>190</sup> so too is patent infringement. And just as “[t]he Lanham Act created a federal protection against [specific] types of unfair competition,”<sup>191</sup> so too did the Patent Act

181. *Roy Export Co.*, 672 F.2d at 1105.

182. *Id.*

183. *Id.* (quoting *Metropolitan Opera Assn. v. Wagner-Nichols Recorder Corp.*, 199 Misc. 786, 796, 101 N.Y.S.2d 483, 492 (Sup. Ct. 1950), *aff’d*, 279 A.D. 632, 107 N.Y.S.2d 795 (1951)).

184. *International News Serv. v. Associated Press*, 248 U.S. 215, 239 (1918).

185. *Electrolux Corp. v. Val-Worth, Inc.*, 6 N.Y.2d 556, 567, 161 N.E.2d 197, 203, 190 N.Y.S.2d 977, 986 (1959).

186. *Metropolitan Opera Assn.*, 199 Misc. at 793, 101 N.Y.S.2d at 489.

187. *Saratoga Vichy Spring Co. v. Lehman*, 625 F.2d 1037, 1044 (2d Cir. 1980).

188. *Whitfield v. Lear*, 751 F.2d 90, 92 (2d Cir. 1984).

189. *Schenk v. Nortron Corp.*, 713 F.2d 782, 786 n.3 (Fed. Cir. 1983). In *Schenk*, the defendant argued that “patents are an exception to the general rule against monopolies.” *Id.* at 784. The court dismissed this argument as “obsfucation.” “The patent right is but the right to exclude others, the very definition of ‘property’ . . . . The antitrust laws, enacted long after the original patent laws, deal with appropriation of what should belong to others. A valid patent gives the public what it did not earlier have.” *Id.* at 786 n.3.

190. *International Order of Job’s Daughters v. Lindeburg & Co.*, 633 F.2d 912, 915 (9th Cir. 1981).

191. *Id.*

of 1952.<sup>192</sup> Therefore, patent infringement may rightfully be considered a specific form of unfair competition.

A patent, however, is a very special creature. The Constitution of the United States specifically provides for the existence of patents.<sup>193</sup> Federal statutes governing patent rights have existed since the beginning of the United States.<sup>194</sup> Has not the federal government preempted the common law of unfair competition insofar as it relates to patents?

A state may not "extend the life of a patent beyond its expiration date or give a patent on an article which lacks the level of invention required for federal patents."<sup>195</sup> Similarly, a state cannot make laws forbidding unfair competition "which give protection of a kind that clashes with the objectives of the federal patent law."<sup>196</sup> A state "may not, when [an] article is unpatented and uncopyrighted, prohibit the copying of the article itself or award damages for such copying."<sup>197</sup>

However, states are not impotent:

Just as the States may exercise regulatory power over writings so may the States regulate with respect to discoveries. States may hold diverse viewpoints in protecting intellectual property relating to invention as they do in protecting the intellectual property relating to the subject matter of copyright. *The only limitation on the States is that in regulating the area of patents and copyrights they do not conflict with the operation of laws in this area passed by Congress . . .*<sup>198</sup>

Therefore, states may recognize patent infringement as a form

192. The Patent Act of 1952, codified at 35 U.S.C. §§ 101-376, was the last major revision to the patent statutes.

193. Congress is empowered "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." U.S. CONST. art. 1, § 8, cl. 8.

194. George Washington signed the first Patent Act on April 10, 1790. See 1 D. CHISUM, PATENTS § 1.01 (1991). Arguing in favor of ratifying the Constitution, James Madison wrote:

The utility of this power will scarcely be questioned. The copyright of authors has been solemnly adjudged, in Great Britain, to be a right of common law. The right to useful inventions seems with equal reason to belong to inventors. The public good fully coincides in both cases with the claims of individuals.

J. MADISON, THE FEDERALIST NO. 43, at 217 (J. Cooke ed. 1982).

195. *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225, 231 (1964); see also *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964).

196. *Sears, Roebuck & Co.*, 376 U.S. at 231.

197. *Id.* at 232-33.

198. *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 479 (1974) (emphasis added).

of "unfair competition" without running afoul of the Supremacy Clause.<sup>199</sup> A state common law of unfair competition which exactly comports with federal patent infringement law is permissible in scope.

### CONCLUSION

Patent infringement is covered under the "Advertising Injury" portion of a CGL insurance policy, and may be considered either "piracy" or "unfair competition" under the language of the policy. Since "advertising" is a necessary and integral part of "selling," and since selling a product protected by a patent will result in liability for patent infringement, the patent infringement "arises out of" the advertising activity.

This interpretation of the CGL policy will not open insurance companies to broad, unexpected liability for patent infringement. Rather, protection is very limited. To be protected as "advertising injury" under a CGL policy, the infringement must be related to advertising. Allegedly infringing articles which would not have been sold "but for" the advertising are covered under the policy. Products which are not sold through advertisements are not covered. Similarly, coverage does not exist for defendants who are accused only of "making" or "using" the patented product or process.

Additionally, coverage will not exist for willful infringement. Although this issue has not been addressed by the courts, it stands to reason that intentional infringement, like any other intentional act, is excluded from coverage.<sup>200</sup>

Finally, providing insurance coverage for patent infringement under the CGL policy will encourage competition. At present, there is a strong incentive to use patents as anti-competitive weapons. Most patents do not issue to individual inventors but to large corporations which can spend large sums of money on research and development.<sup>201</sup>

---

199. "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land . . ." U.S. CONST. art. 6, cl. 2.

200. Willful infringement is commonly pleaded by a patentee, but is rarely successful. A mere allegation of willful infringement should not be sufficient to avoid the insurer's duty to defend. However, a finding that the insured willfully infringed a patent may vitiate the insurer's duty to indemnify.

201. Of course, there are exceptions. One of the most famous recent cases in

A large company which owns a patent has strong incentive to litigate a marginal case of patent infringement against a small competitor because the cost of litigation will force the small company to either go out of business or settle the law suit under onerous terms. For example, Philip Sperber, the vice president and lead litigator for Refac Technical Development Corporation<sup>202</sup> until his death in 1989, stated:

The company with large resources that can afford a \$300,000 counsel fee should not voluntarily put itself on the same bargaining level as a smaller firm it is in a dispute with. It only makes sense to use the cost of litigation as bargaining leverage to force a settlement on terms favorable to the party that can litigate the matter to death without worrying about the cash flow.<sup>203</sup>

As the liberal pleading and discovery rules developed in per-

---

which an individual inventor has "successfully" tackled "corporate America" is *Kearns v. Ford Motor Co.*, 726 F. Supp. 159 (E.D. Mich. 1989). Mr. Kearns developed the intermittent windshield wiper in 1963. *Id.* at 162. His simple device was quickly adopted by the automakers, and is still standard equipment on most automobiles. In 1978, Kearns sued Ford and twenty other automakers for patent infringement. *Id.* at 160.

The suit finally went to trial in January 1990 against Ford. A Detroit jury found infringement and awarded Kearns \$5.2 million, plus interest and attorneys' fees. In the intervening years, however, the suit resulted in Kearns incurring millions of dollars in legal fees and debts, divorcing his wife, having a nervous breakdown and being jailed for his inability to pay alimony. Potts, *Wiper Inventor Wants It All*, Cleveland Plain Dealer, July 29, 1990, at 1E.

202. Refac is a curious result of the new "strengthened" patent system. Refac is a company which purchases marginal patents for the sole purpose of litigating the patents or, as one commentator called it, "patent blackmail." See Andrews, *A 'White Knight' Draws Cries of 'Patent Blackmail'*, The New York Times, Jan. 14, 1990, at F5 col. 1. Refac's president, Eugene M. Lang, a New York philanthropist, made national headlines several years ago when he struck a deal with a class of sixth graders in Harlem: "If they finished high school, he would pay their college expenses." *Id.*

Although retailers and ultimate consumers may be liable for patent infringement, there is a strong hesitation on the part of patent owners to sue the retailers or customers, since those customers of the patent infringer are often the customers of the patent owner as well. This reality of the business world acts as a natural check, preventing patent owners from suing (usually) smaller retailers and customers, rather than the manufacturer who is actually making the infringing product.

This effective immunity of end-users from suit is not present in Refac's cases due to the nature of Refac's business. Since it does not make or sell any products, Refac does not hesitate to sue retailers and end-users for patent infringement. The result is cases in which dozens of small companies with marginal interest in the patent are named as defendants. Rather than litigate the patent issues, they settle with Refac for the "nuisance value" of the meritless suit. W. OLSON, *THE LITIGATION EXPLOSION* 263-64 (1991).

203. Sperber, *Overlooked Negotiating Tools*, 20 LES NOUVELLES 81, 81 (1985).

sonal injury law are increasingly applied to commercial litigation, it becomes easier and easier to file suit.<sup>204</sup> Because of the number and complexity of legal and factual issues involved, even a marginal patent infringement case can be sustained through several years of discovery.<sup>205</sup> As a result, a patent infringement defendant may spend hundreds of thousands of dollars even though it did nothing wrong.

Moreover, a successful defendant has virtually no hope of collecting the attorneys' fees incurred in defending a marginal lawsuit. Under 35 U.S.C. § 285, a prevailing patent infringer can obtain attorneys' fees if the infringement was willful.<sup>206</sup> Thus, a patent owner with limited resources can obtain counsel on a contingent fee basis, and, in theory, be made whole. A defendant, however has no such recourse.<sup>207</sup>

Having an insurer with a duty to defend the accusation of patent infringement will allow the small competitor to litigate the case on its merits. An adjudication on the merits, rather than an adjudication by fiat on economic terms, will foster competition and strengthen the patent system.

204. See generally W. OLSON, *THE LITIGATION EXPLOSION* (1991).

205. In addition to liberalized procedural rules which encourage litigation, there is a perception among many people that the CAFC is "pro-patent," that is, favoring the patent owner in patent infringement suits. Approximately 80% of the patents which reach the CAFC are held valid and infringed. "The number of U.S. patents being held valid and infringed has increased dramatically, injunctions are being granted, and damages verdicts have increased significantly, thus causing an increase in royalty rates under U.S. patents." A. Rose, *U.S. Intellectual Property Law Sees Changes*, 24 *Les Nouvelles* 123, 123 (1989).

In addition, the CAFC has followed the trend in American jurisprudence to avoid clearly delineated "bright line" rules in favor of rules which must examine the "totality of the circumstances." The result is difficulty in evaluating the merits of an infringement suit before trial.

The CAFC is pro-patent because it has created a "penumbra of uncertainty" surrounding the patent claims so that the public rarely knows the scope of the claims "until a district court passes on the issue." . . . [A]n innovator has no warning when a "hypothetical claim" may ensnare him in patent infringement litigation.

Hantman, *Prosecution History Estoppel: Part II*, 73 J. PAT. TRADEMARK OFF. SOC. 234, 254-55 (1991) ("In view of [the doctrine of equivalents], a copier rarely knows whether his product 'infringes' a patent or not until a district court passes on the issue." (referring to the CAFC's statement in *Paper Converting Mach. Co. v. Magna-Graphics Corp.*, 745 F.2d 11, 19 (Fed. Cir. 1984))).

206. "The court in exceptional cases may award reasonable attorney fees to the prevailing party." 35 U.S.C. § 285 (1988).

207. An exception is made in situations where the patent owner has committed fraud in procuring the patent. See, e.g., *Mathis v. Spears*, 857 F.2d 749, 754 (Fed. Cir. 1988).